

1977
Annual Report

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INTERCO 66th Annual Report

Annual Meeting of Stockholders

will convene at 10 a.m. Monday, June 20, 1977 at the Breckenridge Pavilion Hotel, Hawthorne Room, One Broadway, St. Louis, Missouri. Notice of the meeting and proxy statement will be sent to stockholders in a separate mailing.

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Apparel Manufacturing Group

designs, manufactures and distributes a full range of popular-priced branded and private-label sports-wear, casual apparel, and outer garments for men and women. Distribution is national in scope to department stores, specialty shops, and other retail units. Substantial distribution, under private label, is made to large national retail and discount chains. Apparel is produced in 56 manufacturing plants and shipped to customers from 11 major distribution centers.

General Retail Merchandising Group

operates 710 retail stores in most regions of the country, offering a wide assortment of popular-priced products and services to the entire family. General retailing operations include junior department stores, discount stores, men's specialty apparel shops, specialty department stores, and supermarket-type hardware, lumber and building materials stores. Merchandise is provided to the stores from 9 modern regional distribution centers.

Footwear Manufacturing and Retailing Group

styles, manufactures and distributes men's, women's and children's footwear in most major price ranges in the United States and Canada, and manufactures and distributes men's footwear in Australia. There are 33 shoe manufacturing plants and 7 major distribution centers. The company operates 894 retail shoe stores and leased shoe departments in the United States, Australia, Canada and Mexico.

INTERCO is a major manufacturer and retailer of popular-priced consumer products and services represented by three operating groups.

Highlights

Fiscal Years Ended	February 28 1977	February 29 1976	Change
From operations:			
Net sales	\$1,566,432,000	\$1,424,252,000	+ 10.0%
Earnings before income taxes	150,334,000	136,658,000	+ 10.0%
Net earnings	76,759,000	69,027,000	+ 11.2%
Percent of net sales	4.9%	4.8%	
Per share of common stock:			
Fully diluted earnings	\$5.36	\$4.84	+ 10.7%
Dividends	\$1.62 1/2	\$1.47 1/2	+ 10.2%
Financial condition at year end:			
Working capital	\$483,612,000	\$439,728,000	+ 10.0%
Current ratio	4.5 to 1	4.2 to 1	
Total assets	778,038,000	719,344,000	+ 8.2%
Stockholders' equity	568,135,000	510,796,000	+ 11.2%
Return on stockholders' average investment	14.2%	14.2%	
Shares outstanding at year end:			
Common stock	13,886,459	13,727,220	
Preferred stock	136,131	141,327	
Number of stockholders	17,100	18,400	
Number of employees	44,700	45,100	

To Our Stockholders

Fiscal Year Nineteen-Hundred and Seventy-Seven saw INTERCO again reach new performance levels. Net earnings and sales established new records, completing thirteen years of uninterrupted progress for your company. Sales were \$1.57 billion, net earnings were \$76.8 million and fully diluted earnings per share were \$5.36.

The record results for fiscal 1977 again illustrate the merit of our diversification program, management disciplines and the ability to exercise necessary controls. The earnings and sales records were achieved despite sluggish economic activity, severe winter weather during the fourth quarter of our fiscal year, and the extremely competitive retail environment which existed the latter part of the year.

As we enter the 67th year of doing business, the capable and hard-working executives of your company will dedicate themselves to a continuing performance of excellence. On the following pages, you will find photographs of the people who are contributing to the outstanding growth of INTERCO. These include your Board of Directors, Corporate Officers, the men who lead our operating companies, and the administrative staff at INTERCO.

The management in each of our operating companies and at corporate headquarters are highly oriented to results.

They are provided the opportunity, the responsibility and the rewards required to accomplish our budgeted goals. Regular communication at our company is a top priority. Our monthly forecasting and budgeting, plus our monthly Operating Board meetings provide the disciplines for constantly measuring performance, including return on assets employed, inventory turnover, exchange of marketing trends and the sharing of the newest manufacturing and retailing techniques.

The quarterly dividend rate on common stock was increased twice during the last nine months—with the July 1976 payment and with the April 1977 payment. The current annual rate is \$1.80 per share—an increase of 18.4% from nine months ago. INTERCO has had sixty-six years of common stock dividends without interruption and twelve consecutive years in which the dividend rate was increased. As earnings continue to grow, the Board of Directors will make frequent reviews of the dividend rate.

Our program of diversification and expansion through profitable acquisitions continued in fiscal 1977. On June 30, 1976, Stuffed Shirt/Stuffed Jeans, Inc., a manufacturer and distributor of junior women's sportswear, joined the Apparel Manufacturing Group, and on January 31, 1977, Sky City Stores, Inc., a chain of large discount centers in the Southeast, became a part of the General Retail Merchandising Group. A complete report on these two fine companies is shown on pages 10 through 13 of this report. Careful diversification and expansion through acquisition will continue to be a part of our planned growth program.

INTERCO is a major manufacturer and retailer of popular-priced consumer products and services, geared to continue profitable growth in every phase of its business.

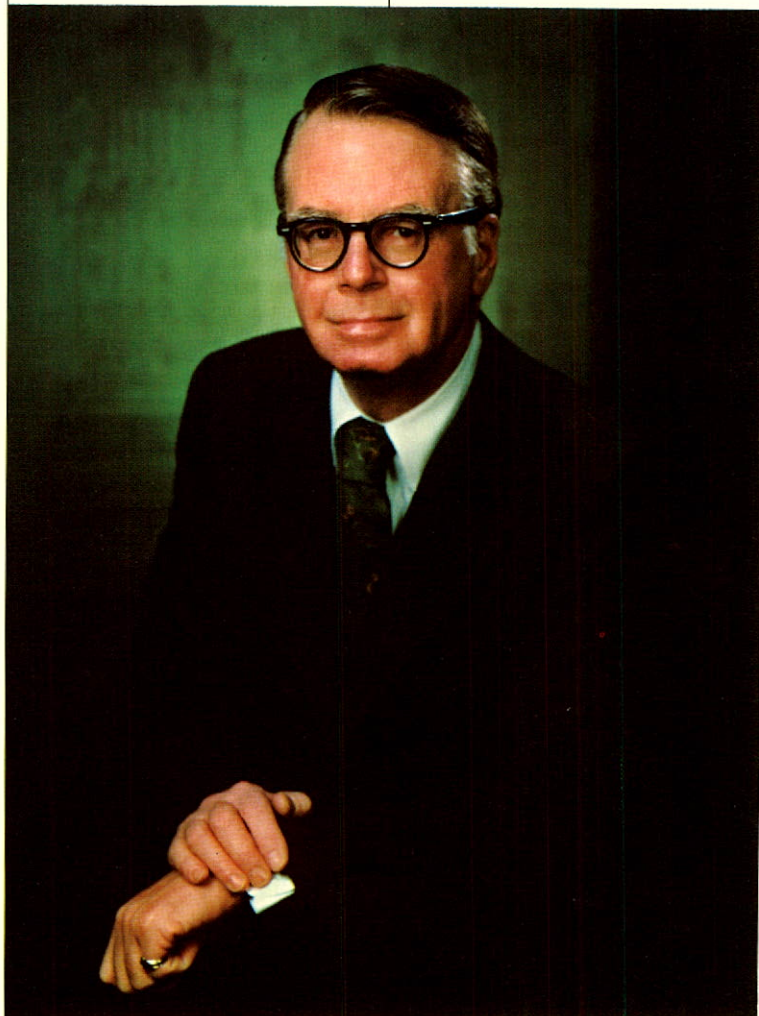
As we enter fiscal 1978, INTERCO is well-positioned in the popular-priced consumer markets with quality products and services. We will continue to assure sound employment of our assets, to maintain our aggressive cost control program and improve our present strong financial structure. We expect fiscal 1978 to be another good year for your company.

This is the first Annual Report since I was elected Chairman of the Board and Chief Executive Officer of INTERCO, and it is a personal privilege for me to extend appreciation to our many loyal customers, to our shareholders who express their confidence by investment, and to our employees for helping make fiscal 1977 another record year.

W. L. Edwards, Jr.

Chairman of the Board
and Chief Executive Officer

April 12, 1977



William L. Edwards, Jr.

Fiscal 1977 in Review

Fiscal 1977 was the 13th consecutive year in which INTERCO has reported new records in both sales and earnings—each year a new high.

Net sales were \$1.57 billion, net earnings were \$76.8 million and fully diluted earnings per share were \$5.36.

Our average compounded annual growth rate, restated, over the past five years was 8.3% for sales, 13.4% for net earnings, and 12.8% for earnings per common share. In addition to the growth performance, the profitability of the company—net earnings to net sales—has improved to 4.9%.

The company's fiscal year ends on the last day in February. In this annual report, all reference to fiscal 1977 refers to the fiscal year ended February 28, 1977, and fiscal 1976 refers to the fiscal year ended February 29, 1976.

The comparative financial statements and references to fiscal 1976, shown in this review, have been restated to include the combination of Sky City Stores, Inc., on a pooling of interests basis.

The following presents our three operating groups' sales and earnings for a five-year period. These figures have been restated to include pooled companies for years prior to their acquisition.

	Fiscal Years Ended				
	1977	1976	1975	1974	1973
Net sales:					
Apparel	576,019	484,152	469,171	427,764	373,866
General Retail	498,557	474,230	425,688	399,507	371,989
Footwear	491,856	465,870	478,364	477,603	442,571
Total	<u>\$1,566,432</u>	<u>\$1,424,252</u>	<u>\$1,373,223</u>	<u>\$1,304,874</u>	<u>\$1,188,426</u>
Earnings before income taxes:					
Apparel	80,750	65,865	54,166	49,039	40,919
General Retail	31,165	34,304	27,862	27,008	20,927
Footwear	49,603	44,683	51,370	45,697	43,642
Total	<u>161,518</u>	<u>144,852</u>	<u>133,398</u>	<u>121,744</u>	<u>105,488</u>
Less corporate expenses and interest cost	(11,184)	(8,194)	(11,473)	(10,426)	(8,077)
Total	<u>150,334</u>	<u>136,658</u>	<u>121,925</u>	<u>111,318</u>	<u>97,411</u>
Income taxes	73,575	67,631	60,255	54,144	48,136
Net earnings	<u>\$ 76,759</u>	<u>\$ 69,027</u>	<u>\$ 61,670</u>	<u>\$ 57,174</u>	<u>\$ 49,275</u>
As a percent of sales	<u>4.9%</u>	<u>4.8%</u>	<u>4.5%</u>	<u>4.4%</u>	<u>4.1%</u>

Sales

Net sales for the year were a record \$1.57 billion, an increase of \$142.1 million or 10.0% over the restated volume of \$1.42 billion for fiscal 1976. Net sales of \$1.38 billion were reported last year.

The sales contribution by the operating groups of the company is compared in millions of dollars:

	Fiscal 1977		Fiscal 1976		% Change
	Sales	%	Sales	%	
Apparel	\$ 576.0	36.8	\$ 484.2	34.0	+ 19.0
General Retail	498.5	31.8	474.2	33.3	+ 5.1
Footwear	491.9	31.4	465.9	32.7	+ 5.6
	<u>\$1,566.4</u>	<u>100.0</u>	<u>\$1,424.3</u>	<u>100.0</u>	<u>+ 10.0</u>

Each of our three operating groups contributed record high sales in the fiscal year ended February 28, 1977, and each group represented approximately one-third of INTERCO's business.

The net sales of the company, by quarters, in millions of dollars were:

	<u>Fiscal 1977</u>	<u>Fiscal 1976</u>
First quarter	\$ 376.5	\$ 317.6
Second quarter	401.5	346.2
Third quarter	397.7	382.2
Fourth quarter	390.7	378.3
	<u>\$1,566.4</u>	<u>\$1,424.3</u>

Earnings

Earnings before income taxes for fiscal 1977 were a record \$150.3 million, showing an increase of \$13.6 million, or 10.0% higher than the restated fiscal 1976 pre-tax earnings of \$136.7 million. Pre-tax earnings reported in fiscal 1976 were \$132.7 million.

Pre-tax earnings of each operating group, before corporate expenses and interest cost, are compared in millions of dollars:

	<u>Fiscal 1977</u>		<u>Fiscal 1976</u>		<u>%</u>
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>	<u>Change</u>
Apparel	\$ 80.7	50.0	\$ 65.9	45.5	+ 22.6
General Retail	31.2	19.3	34.3	23.7	- 9.2
Footwear	49.6	30.7	44.7	30.8	+ 11.0
	<u>\$161.5</u>	<u>100.0</u>	<u>\$144.9</u>	<u>100.0</u>	<u>+ 11.5</u>

Our Apparel Manufacturing Group, representing 50.0% of the earnings of INTERCO for fiscal 1977, had a record year—both men's and women's apparel. Our General Retail and our Footwear Manufacturing and Retailing Groups' earnings were the second highest of any fiscal year for each of the two groups. We were pleased with the performance and the improved earnings of our Footwear Manufacturing and Retailing Group over last year. The current year's footwear earnings were only slightly less than the record results of two years ago. The earnings of our General Retail Group fell below the record and very strong performance of last year. This was attributable to above normal markdowns plus a higher cost of doing business.

Net earnings for the year were a record \$76.8 million, an increase of 11.2% over the restated net earnings of \$69.0 million in the previous year. The reported net earnings for fiscal 1976 were \$67.0 million. The company's margin of profitability—net earnings to net sales—was 4.9% for fiscal 1977 compared with 4.8% restated for the prior year.

Fully diluted earnings per common share were \$5.36 for fiscal 1977, an increase of \$0.52 per share or 10.7% over restated \$4.84 per share earnings in fiscal 1976. Fully diluted earnings per common share reported for fiscal 1976 were also \$4.84.

Net earnings and fully diluted earnings per common share for each quarter are compared in the following:

	<u>Net Earnings (In millions)</u>		<u>Net Earnings per Share</u>	
	<u>Fiscal 1977</u>	<u>Fiscal 1976</u>	<u>Fiscal 1977</u>	<u>Fiscal 1976</u>
First quarter	\$15.9	\$12.3	\$1.11	\$0.87
Second quarter	17.1	14.5	1.20	1.01
Third quarter	21.0	20.4	1.46	1.43
Fourth quarter	22.8	21.8	1.59	1.53
	<u>\$76.8</u>	<u>\$69.0</u>	<u>\$5.36</u>	<u>\$4.84</u>

Fiscal 1977 in Review

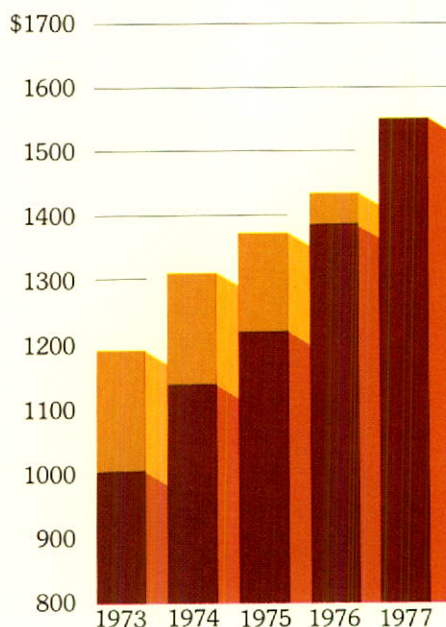
Financial Position

INTERCO's very strong financial position continued to grow during the 1977 fiscal year.

- The working capital of the company—the excess of current assets over current liabilities—was another record high at \$483.6 million on February 28, 1977—an increase of \$43.9 million over the previous year. The working capital ratio was 4.5 to 1 at the end of fiscal 1977. Our working capital has increased over the past five years at an average compounded annual rate of 9.6%.
- Cash and marketable securities were \$94.8 million compared with \$90.7 million one year ago, after financing higher inventories and accounts receivable, and a record capital expenditure program. Short-term foreign bank borrowings, required by our Canadian subsidiary, were \$7.4 million at year-end.
- Accounts receivable were \$189.9 million at February 28, 1977—higher by 6.6%, and inventories were \$328.6 million—up 8.4%, each reflecting the increased level of our business and they are in line with our forecasted levels.
- Long-term debt, less current maturities, was \$58.4 million at February 28, 1977, which is 10.3% of the stockholders' equity of the company. The slight increase in our long-term debt is the result of capitalizing certain leases and the debt acquired in an acquisition during the current year.
- Stockholders' equity has increased over the past five years at an average compounded annual rate of 11.3%. Stockholders' equity was \$568.1 million at February 28, 1977—up 11.2% from \$510.8 million at the end of fiscal 1976. Book value per common share increased to \$39.93 from \$36.18 one year ago. The return on average stockholders' equity was 14.2% for fiscal 1977.

Net Sales

Millions of Dollars

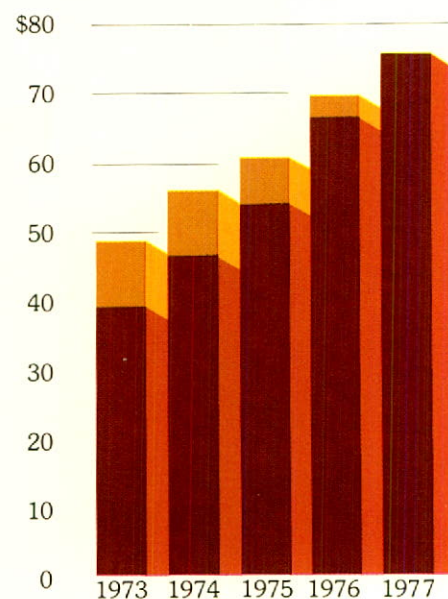


■ As reported

■ Restated for companies acquired on a pooling of interests basis for years prior to their affiliation.

Net Earnings

Millions of Dollars



■ As reported

■ Restated for companies acquired on a pooling of interests basis for years prior to their affiliation.

Capital Expenditures

Record high capital expenditures of \$28.7 million were made during fiscal 1977, bringing the amount spent for expansion, improvements, and modernization over the past five years to \$118.0 million. Depreciation in fiscal 1977 was \$16.7 million. The expenditures in fiscal 1977 included new retail stores, new manufacturing plants and customer distribution centers and, in addition, the refurbishing of several of our retail relocations, new equipment, and the modernization of plant facilities.

Capital expenditures for the new fiscal year are budgeted at \$20.0 million with depreciation estimated to be \$18.0 million.

Dividends

Fiscal 1977 was the 12th consecutive year of increased common stock dividends, and the 66th consecutive year of cash dividend payments. Cash dividends of \$22.7 million were paid during the fiscal year, with \$21.7 million to holders of common stock and the remainder to holders of preferred stock and by the pooled company prior to combination.

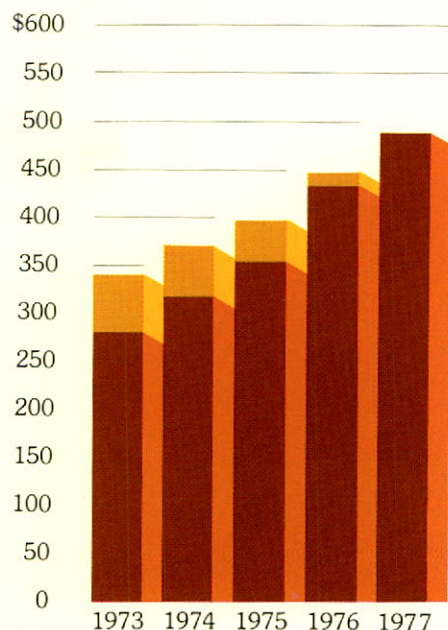
Quarterly common stock cash dividends per share were paid as follows:

	Fiscal 1977	Fiscal 1976
First quarter.....	\$0.38	\$0.36½
Second quarter.....	0.41½	0.36½
Third quarter.....	0.41½	0.36½
Fourth quarter.....	0.41½	0.38

The quarterly dividend rate on common stock is presently \$0.45 per share or an annual rate of \$1.80 per common share, effective with the April 15, 1977 payment.

Working Capital

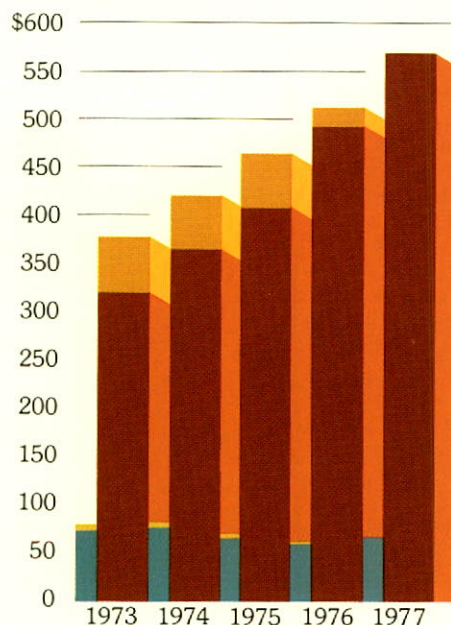
Millions of Dollars



- As reported
- Restated for companies acquired on a pooling of interests basis for years prior to their affiliation.

Stockholders' Equity and Long-Term Debt

Millions of Dollars



- Stockholders' Equity
- Long-Term Debt
- Restated for companies acquired on a pooling of interests basis for years prior to their affiliation.

Fiscal 1977 in Review

Common Stock

The stockholders approved an increase in the authorized number of shares of common stock from 30 million to 50 million shares at the June 21, 1976 annual meeting. There are no present plans for the use of this additional stock. On February 28, 1977, there were 13,886,459 shares of common stock outstanding, and the closing market price of INTERCO's common stock on that date was \$40.50 per share.

The market price range per share of the company's common stock, as quoted on the New York Stock Exchange, is shown as follows:

	Fiscal 1977		Fiscal 1976	
	High	Low	High	Low
First quarter	\$48 ³ / ₈	\$40 ¹ / ₈	\$35 ⁷ / ₈	\$26 ¹ / ₄
Second quarter	43 ¹ / ₂	39 ⁷ / ₈	39 ¹ / ₄	28
Third quarter	44 ¹ / ₂	40 ³ / ₄	40 ³ / ₄	29 ³ / ₄
Fourth quarter	46 ¹ / ₄	40	48	37

After the close of the fiscal year, 136,131 outstanding shares of Second Preferred Stock, Series C, were converted into 415,643 shares of common stock. There are currently no shares of the company's preferred stock outstanding.

Acquisitions

- Stuffed Shirt/Stuffed Jeans, Inc. was acquired for cash on June 30, 1976, and its results of operations are included herein from that date.
- Sky City Stores, Inc. was acquired on January 31, 1977 in an exchange of 427,079 shares of INTERCO common stock for all of the outstanding capital stock of Sky City and was accounted for as a pooling of interests.

New Chief Executive Officer

On June 21, 1976, William L. Edwards, Jr. was elected Chairman of the Board of Directors and Chief Executive Officer of the company, succeeding Maurice R. Chambers.

Mr. Edwards joined the company in 1969, and has served as Vice President of Finance, Executive Vice President, and Vice Chairman of the Board and Chief Administrative Officer.

Mr. Chambers became Chairman of the Executive Committee of the Board of Directors on June 21, 1976. He served as Chief Executive Officer of the company for more than fourteen years, leading it to new and significant achievements each year. His contribution to the growth of the company has been outstanding.

Executive Appointments

- William Forman became Chairman of the Board of Devon Apparel, Inc. on January 3, 1977, after serving as President for many years.
- Arthur Sibley was elected President of College-Town, Inc. on January 27, 1977, succeeding the late Gerald Sibley. Arthur Sibley had been Executive Vice President of College-Town.

Operating Board Appointments

The following were appointed to the ever-important Operating Board of the company during the year:

- Gerald B. Hirsch, President of P. N. Hirsch & Company, replacing Philip N. Hirsch, who is Chairman of the Board of P. N. Hirsch & Company.
- Harvey Rothenberg, Chairman of the Board of Stuffed Shirt/Stuffed Jeans, Inc.
- Arthur Sibley, President of College-Town, Inc.
- Myron C. Peterson, Chairman of the Board and President of Sky City Stores, Inc.

Five-Year Summary

The Five-Year Consolidated Financial Review on page 40 is a detailed presentation of the company's steady growth. The comparisons are particularly significant since they reflect the internal growth of the operations of the companies which constitute INTERCO's expanded base of operations.

Form 10-K—Annual Report

A copy of INTERCO INCORPORATED's current 10-K Report filed with the Securities and Exchange Commission, can be obtained by any shareholder by writing to: Treasurer, INTERCO INCORPORATED, Ten Broadway, St. Louis, Missouri 63102

Trademarks

The trademarks of INTERCO INCORPORATED and its subsidiaries, where used in the Annual Report, are italicized.

Shown are the Administrative Officers of INTERCO

who meet weekly to coordinate corporate matters: Seated, left to right: Duane A. Patterson, Secretary; John K. Riedy, President and Chief Operating Officer; William L. Edwards, Jr., Chairman of the Board and Chief Executive Officer; Ronald L. Aylward, Vice President and General Counsel. Standing, left to right: Russell L. Baumann, Assistant Controller—Manager of Internal Auditing; William R. Withrow, Assistant Treasurer—Manager of Taxes; Stanley F. Huck, Controller; Edward P. Grace, Treasurer.



Stuffed Shirt/ Stuffed Jeans, Inc. joins INTERCO

Stuffed Shirt/Stuffed Jeans, Inc. joined the Apparel Manufacturing Group of the company on June 30, 1976.

This company commenced operations in 1964, quickly became a factor in the junior women's shirt field, and subsequently entered the junior women's jean business.

Today, they are a major designer, manufacturer and distributor of jeans, pants, shirts and T-shirts in the moderate-priced category for the young junior and junior women's market. The company specializes in providing color-related sportswear to more than 3,000 department stores and specialty stores throughout the United States, under the brand names of *Stuffed Shirt* and *Stuffed*

Jeans. The company also makes substantial unbranded distribution to national retailers and national mail order chains.

Design, merchandising and marketing facilities and showrooms are in New York City, with production plants located in Pass Christian, Mississippi and Slidell, Louisiana. A new, fully-automated customer distribution center in Long Beach, Mississippi was completed within the past year.

Additional prospects for growth will be possible with the creation in April, 1977 of a separate sales division—*Stuff Sportswear*—for the junior woman. This new sales division will produce and offer a collection of related separates—"switchables"—tops and bottoms.

Stuffed Shirt/Stuffed Jeans' product identification and the discriminating junior woman's acceptance, together with an excellent management team, again expands INTERCO's growth opportunities in the women's apparel business.



**Stuffed
Shirt.** **STUFFED**
JEANS
WORK TOGETHER



... and Sky City Stores, Inc. Merges With INTERCO

Sky City Stores, Inc., a multi-state retailer of 41 giant discount centers, headquartered in Asheville, North Carolina, became a part of the General Retail Merchandising Group of INTERCO on January 31, 1977.

Since the first Sky City Discount Center opened in 1962, growth has been a constant factor as the company expanded its marketing area. Presently, the self-service chain has large retail centers in North Carolina, South Carolina, Georgia, Tennessee and Alabama. Long-range plans include a steady, orderly expansion program to be executed in response to economic assessments and customer needs in the region.

Present plans include six additional locations for fiscal 1978.

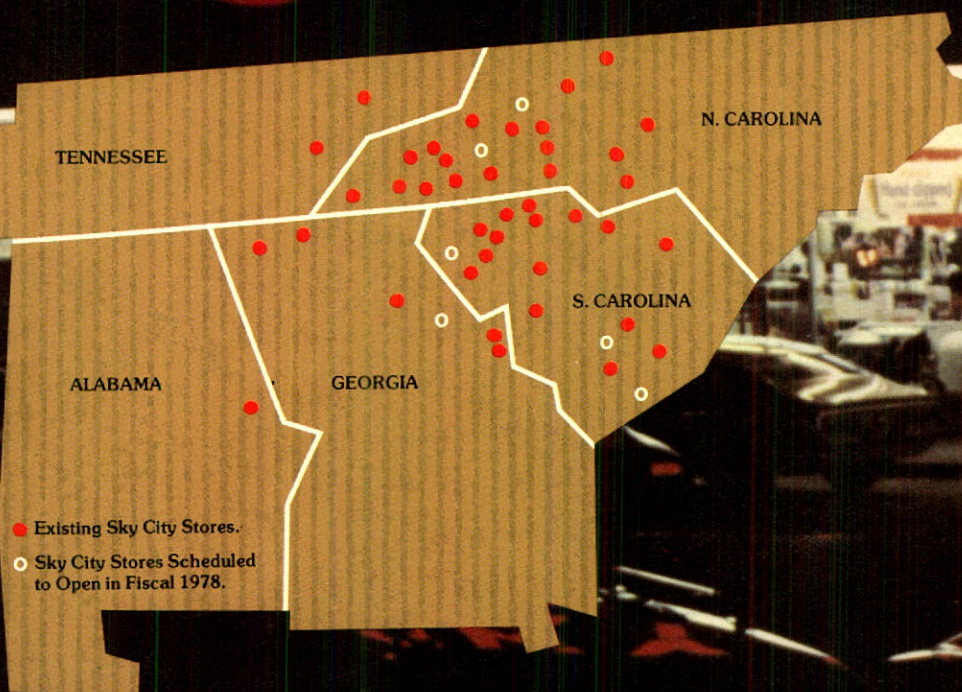
Sky City Discount Centers, averaging 45,000 square feet, carry a wide assortment of popular-priced merchandise at competitive prices, aggressively advertised. The principal offerings for the consumer are apparel for the family, sporting goods, small and major appliances, home furnishings, hardware, health and beauty aids, footwear, jewelry, toys, lawn and garden supplies, automotive accessories, and products for the "do-it-yourself" homeowner.

Maintaining a steady growth rate and a high stand-

ard of retail service requires a well-grounded, well-balanced management team. Sky City's management group has thorough knowledge in their field, knowledge gained from many years' experience in retailing.

Sky City Stores, Inc. allows INTERCO to extend its base of operations into a new geographical region for its popular-priced retailing, and brings new opportunity for future growth in the Southeastern region of the country.

SKY CITY





Apparel Manufacturing Group

The Apparel Manufacturing Group had a banner year in fiscal 1977, again reporting record sales and record earnings—in both the women's and the men's portions of our business.

The Apparel Group contributed \$576.0 million or 36.8% of the consolidated sales and \$80.7 million or 50.0% of the earnings for a return on sales of 14.0% before income taxes, corporate expense and interest cost. The sales increase amounted to 19.0%, and the earnings gain before taxes, corporate expenses and interest cost was 22.6%.

During the past year, apparel plant capacity and customer distribution centers were each increased 10% to accommodate the continuously

increasing consumer demand for INTERCO's casual apparel and sportswear lines. In addition, we continue to seek the latest improvements in manufacturing equipment, and have a regular program of machinery replacement that includes the acquisition of the newest in automation.

Women's Apparel Manufacturing

INTERCO's widely accepted women's apparel brands are shown on pages sixteen and seventeen of this report. Our moderately-priced clothing for women serves three distinct markets—the young junior, the junior, and the more sophisticated look for the missy market offering

suits, dresses, pants, skirts, jackets, sweaters, blouses, shirts, T-shirts, jumpers, vests, jeans, culottes, blazers, rainwear, golf jackets, and light and heavy outerwear.

Quality sportswear and casual women's clothing, whether tailored or active, basic or a fashion image, is in great demand. By emphasizing quality control, and today's life style and fashion-forward styling, we will increase our share of this expanding market.

Women's Apparel: Seated, left to right: Arthur Sibley, President, College-Town, Inc.; Harvey Saligman, President, Queen Casuals, Inc. Standing, left to right: Stanley Matzkin, President, Devon Apparel, Inc.; Sidney Gould, Chairman, Sidney Gould Co. Ltd.; Harvey Rothenberg, Chairman, Stuffed Shirt/Stuffed Jeans, Inc.



Men's Apparel Manufacturing

INTERCO produces a full range of moderately-priced casual apparel, sportswear and outerwear for the male consumer of all ages, which includes shirts—sport, knit, and dress—slacks, sweaters, sport coats, blazers, three-piece vested casual sport suits, jeans, western wear, golf jackets, rainwear, light and heavy outerwear, walk shorts and swimwear.

Our men's apparel offerings cater totally to the new life-style and to the fashion-conscious male consumer with everything from classic casual to the rugged look, a few of which are shown on pages eighteen and nineteen of this report.

Londontown Corporation, featuring its famous *London Fog* trademark, completed its first full year with INTERCO, establishing new records in sales and earnings, and will introduce in the Fall of 1977 an exciting new *London Fog* leather outerwear program.

Also in the new year, we will provide new unbranded distribution by manufacturing moderately-priced western jeans for merchandising in the Western European market, adding to our apparel customer base.

General

The leaders of our apparel companies, pictured below, and their associates, have made a significant contribution

to the outstanding growth of INTERCO's apparel manufacturing business. They are prepared to accept future challenges, remaining alert to the dynamic style-setting demands of the apparel consumer.

Men's Apparel: Seated, left to right: William B. Cowden, President, Cowden Manufacturing Company; Charles J. Rothschild, Jr., President, Campus Sweater & Sportswear Company; Lionel Baxter, President, Big Yank Corporation. Standing, left to right: Saul Brodsky, Chairman, The Biltwell Company, Inc.; Jonathan P. Myers, President, Londontown Corporation.



Apparel
Manufacturing
Group

college town

devon.



LADY
QUEEN.

independents



it's
pure
gold

**Major Apparel Brands for
Women and Young Women:**
*Clipper Mist • College-Town •
 Devon • Independents •
 It's Pure Gould • Lady Devon •
 Lady Queen • London Fog •
 Pant-her • Queen Casuals •
 Stuffed Jeans • Stuffed Shirt •
 Stuff Sportswear.*

pant'her ♡



London Fog®



lady
devon.

**QUEEN
 CASUALS.**



Apparel
Manufacturing
Group

COWDEN

Studio One
by CAMPUS



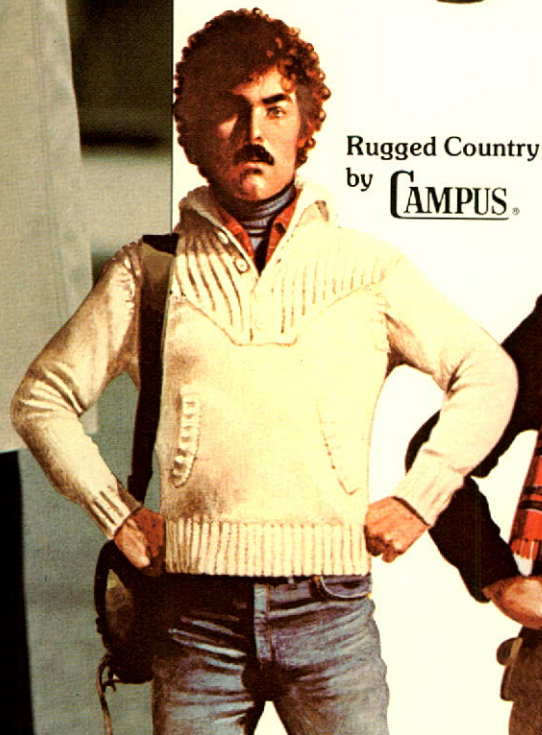
London Fog®

Major Apparel Brands for Men and Young Men:

Big Yank • Biltwell •
 Campus • Clipper Mist •
 Concept II by Campus •
 Cowden • Esprit by Campus •
 Joe College by Campus •
 John Alexander • Leonard Macy •
 London Fog •
 Mr. Golf • Mr. Tennis •
 Pro-action by Campus •
 Rugged Country by Campus •
 Startown • Studio One by Campus •
 Tailor's Bench •
 Yankee Gear.



BIG YANK



Rugged Country
by **CAMPUS®**



General Retail Merchandising Group

Sales were a new record in fiscal 1977, and earnings were the second highest since our entry into the general retailing business in 1964. The earnings fell below the record and very strong performance of last year as a result of above-normal markdowns in a portion of our junior department stores' business, and a higher cost of doing business. Record sales and earnings, however, were posted for the year in our discount centers, and supermarket hardware and lumber stores.

The General Retail Group contributed \$498.5 million or 31.8% of the total sales volume, and \$31.2 million or 19.3% of the earnings, a return on sales of 6.3% before income taxes, corporate expenses and interest cost. The sales increase was 5.1%, and the earnings reduction before

taxes, corporate expenses and interest cost was 9.2% from the record earnings base established one year ago.

Maintaining our expansion program for this important part of the business, 46 new locations were opened during the past fiscal year, with some relocations and closings. In addition, the profit base of the General Retail Group was expanded in fiscal 1977 by the acquisition of Sky City's 41 giant supermarket discount centers which permitted a market penetration in the Southeastern region of the United States, and future expansion opportunities.

The divisions within the General Retail Group offer a wide variety of popular-priced products and services—everyday necessities—for the quality-conscious and cost-

conscious consumer. Data recording terminals have been introduced in many of our new stores and are being phased into existing locations to provide management with swift decision-making information to increase inventory turnover, margins and in-stock ratios, and to improve on our efficient and economical service to our customers.

Seated, left to right: Gerald B. Hirsch, President, P. N. Hirsch & Company; John Weil, President, Eagle Family Discount Stores, Inc.; Stanley M. Cohen, President, Central Hardware Company; Myron C. Peterson, Chairman and President, Sky City Stores, Inc. Standing, left to right: Barry S. Fine, President, Fine's Men's Shops, Inc., and Standard Sportswear, Inc.; Edward S. Golde, President, Golde's Department Stores, Inc.



• *P. N. Hirsch & Company*, our 389 unit junior department store chain, had its traditional earnings improvement record sidetracked during fiscal 1977 from excessive markdowns, principally in its Southern division. All other divisions of the *Hirsch* company—the Midwest, the Northwest, Texas and California, performed satisfactorily during the year. Inventories in the Southern area are in line, and *P. N. Hirsch & Company* should resume its upward movement through aggressive merchandising programs.

• *Central Hardware*, operating 24 supermarket stores, achieved another record year in both sales and earnings, responding to the increasing demands of the “do-it-yourself” homeowner. In addition, special emphasis has been introduced on home comfort, home security and energy saving applications for the homeowner. *Central Hardware*, expanding its retailing potential, will enter the metropolitan Cincinnati, Ohio “do-it-yourself” market during fiscal 1978 with two giant supermarket type stores.

• *Eagle Family Discount Stores*, with 173 Florida locations, continued its growth with record sales and earnings in fiscal 1977. It will bring its merchandising expertise for everyday, low-priced consumer necessities to other communities in the coming year with the addition of twenty new locations.

• *Fine's, Standard, and United*—INTERCO's chain of 76 men's specialty apparel shops—had a satisfactory year providing the fashion conscious male consumer with an extensive selection of merchandise, from tailored apparel to sportswear, and accessories.

• *Golde's*, which operates seven specialty department stores, is researching

midwestern communities, and is planning further expansion in fiscal 1978.

Shown on page twenty are the chief operating officers of our general retailing companies. These men are outstanding retailers, and through their excellent guidance, INTERCO's general retail business will expand and grow in the years ahead.

The General Retail Group's long-term strategy is catering to middle-income America, and it will continue to maintain and expand this goal with competitive prices for needed products.

P. N. HIRSCH & CO.



General Retail
Merchandising
Group

"Eighty-seven new general
retailing units, offering
popular-priced consumer
products and services, were
added during the year. . ."





Major Retail Trading Names:
 Central Hardware • Carithers •
 Eagle Family Discount Stores •
 Fine's Men's Shops •
 Golde's Department Stores •
 Hirsch Value Centers •
 Idaho Department Stores •
 Jeans Galore • Keith O'Brien •
 Kent's • Miller's •
 P.N. Hirsch Department Stores •
 Shainberg's •
 Sky City Discount Centers •
 Standard Sportswear •
 Thornton's • United • Wigwam.



Footwear Manufacturing and Retailing Group

Despite another uncertain and erratic year for the shoe industry, the Footwear Group posted record sales, and its earnings were the second highest in the long history of the footwear business of INTERCO.

The Group contributed \$491.9 million or 31.4% of the consolidated sales, and \$49.6 million or 30.7% of the earnings of the company. This was a 10.1% profit on sales before income taxes, corporate expenses and interest cost. The sales increase amounted to 5.6%, and the earnings gain from one year ago before taxes, corporate expenses and interest cost was 11.0%.

Footwear Retailing

Our retail footwear business had improved sales and earnings over the previous year, and at the end of the fiscal year there were 894 shoe

stores and leased shoe departments in operation. These included 65 new locations opened during the year in large regional malls and other selected prestige locations in the United States, Canada, Mexico and Australia. A number of marginally profitable retail units were closed during the year.

Shown on page twenty-seven are two of the luxurious stores of the many independent shoe retailers who participate in the growing *Florsheim Dealer Development Program*, which assists retail shoe dealers in major store remodeling and new store design and construction, and provides operational assistance in achieving maximum profitability.

Expansion will continue in fiscal 1978, which will include *Florsheim Shoe Shops for Men*, leased shoe departments

in leading clothing and department stores, and *Florsheim Thayer McNeil Shops* which feature *Florsheim* shoes for women and/or men.

Footwear Manufacturing

Consumer and retail demand for INTERCO's quality footwear—dress and work shoes, casual footwear and boots for men, women and children—resulted in improved sales and earnings in fiscal 1977. Continuous new product development and improved manufacturing techniques, coupled with up-to-the-minute design to meet

Left to right: J. Carl Powers, President, International Shoe Company; Jack Spewak, President, Senack Shoes, Inc.; Donald G. MacLeod, President, Interco Savage Limited; Richard P. Hamilton, President, The Florsheim Shoe Company.



fast-changing style trends, maintains our footwear manufacturing business as one of the leading shoe producers in this country, despite the continuous increased competition from foreign-made footwear.

• *The Florsheim Shoe Company*, in addition to maintaining and increasing its position as a leader of quality leather footwear for men and women, is extensively promoting its growing *Idlers* collection of quality casual and leisure footwear for men and women, capitalizing on the growth in this segment of the market. *Florsheim* is also benefiting from its export activities which, through independent retailers, places more *Florsheim* shoes each year in major metropolitan retail areas of many foreign countries.

• *International Shoe Company*, with its strong merchandising, strict cost

Patriot Athletic Footwear for Men, Women, and Children

control, and new product development, had another excellent year in fiscal 1977. In addition to its complete lines for men, women and children, *International Shoe* has expanded its very successful *Hy-Test Safety Shoe* styling to afford dual use by the consumer for work and leisure. A completely new line, *Patriot Athletic Footwear* for men, women and children, was successfully introduced during the year. Also, a new young women's line—*Crawdads*—was introduced for

the jean generation, and its acceptance is on target.

• *Interco Savage Limited*, manufacturer of men's, women's and children's shoes for the Canadian market, increased their position during the year, operating at a higher profit level.

• *Senack Shoes, Inc.*, primarily operators of leased shoe departments, had a very good year and will expand its operating base in fiscal 1978.

General

Pictured on page twenty-four are the chief operating officers of each of our footwear

divisions, who have led their companies to new excellence in maintaining *INTERCO's* position as a principal manufacturer of quality footwear, and in providing growth in retail distribution to independent shoe retailers, department stores, national chains, and *INTERCO's* own retail shoe operations.



HY-TEST.
Safety Shoes



RAND.
Ambassador.
WINTHROP.



VITALITY.
DIVINA.
Personality.
Miss Wonderful.

by **International Shoe Company**

Footwear Manufacturing and Retailing Group

Florsheim Shoes
for Women





**IDLERS
BY FLORSHEIM®**

Major Footwear Brands:

For Men: Ambassador • City Club • Florsheim—Florsheim Imperial and Royal Imperial • Hy-Test • Idlers by Florsheim • Julius Marlow • McHale • Patriot • Rand • Roberts • Winthrop • Worthmore.

For Women: Crawdads • Denny Stewart • diVina • Florsheim • Idlers by Florsheim • Miss Wonderful Patriot • Personality • Thayer McNeil • Savage Casuals • Thomas Wallace • Vitality.

For Children: Red Goose • Patriot • Poll Parrot • Savage.

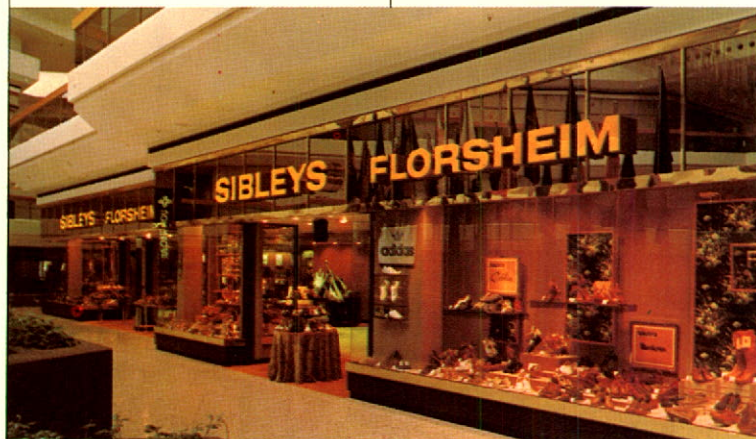
Major Retail Trading Names:

Florsheim Shoe Shops for Men • Florsheim Thayer McNeil Men's and Women's Shops • Duane's • Gude's • Paul's Shoes • Phillips Shoes • Thayer McNeil Shoes • Thompson, Boland & Lee.

FLORSHEIM®

**Florsheim Dealer
Development Program**

**"Sixty-five new locations
opened during the year in
large regional malls and
other selected prestige
locations. . ."**



Consolidated Balance Sheet

(Dollars in thousands)

ASSETS

	February 28 1977	February 29 1976
Current assets:		
Cash	\$ 5,856	\$ 6,107
Marketable securities	88,933	84,595
Receivables, less allowances of \$9,567 (\$8,460 in 1976) . . .	189,943	178,129
Inventories	328,624	303,199
Prepaid expenses and other current assets	<u>9,475</u>	<u>7,122</u>
Total current assets	622,831	579,152
Property, plant and equipment	255,839	235,497
Less accumulated depreciation	<u>120,225</u>	<u>113,178</u>
Net property, plant and equipment.	135,614	122,319
Other assets	<u>19,593</u>	<u>17,873</u>
	<u>\$778,038</u>	<u>\$719,344</u>

See accompanying notes to consolidated financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY

	February 28 1977	February 29 1976
Current liabilities:		
Foreign bank borrowings	\$ 7,436	\$ —
Current maturities of long-term debt	4,778	4,113
Accounts payable and accrued expenses	106,644	116,724
Income taxes	<u>20,361</u>	<u>18,587</u>
Total current liabilities	139,219	139,424
Long-term debt, less current maturities	58,371	56,993
Other long-term liabilities	12,313	12,131
Stockholders' equity:		
Preferred stock, at stated and liquidating value	13,613	14,133
Common stock, at stated value	104,148	102,954
Capital surplus	39,710	36,341
Retained earnings	<u>410,664</u>	<u>357,368</u>
Total stockholders' equity	<u>568,135</u>	<u>510,796</u>
	<u>\$778,038</u>	<u>\$719,344</u>

Consolidated Statement Of Earnings

(Dollars in thousands except per share data)

	Years Ended	February 28 1977	February 29 1976
Income:			
Net sales		\$1,566,432	\$1,424,252
Other income, net		<u>16,414</u>	<u>14,988</u>
		<u>1,582,846</u>	<u>1,439,240</u>
Costs and expenses:			
Cost of sales		1,094,849	992,778
Selling, general and administrative expenses.		333,475	306,094
Interest expense		<u>4,188</u>	<u>3,710</u>
		<u>1,432,512</u>	<u>1,302,582</u>
Earnings before income taxes.		150,334	136,658
Income taxes		<u>73,575</u>	<u>67,631</u>
Net earnings		<u>\$ 76,759</u>	<u>\$ 69,027</u>
Per share of common stock:			
Fully diluted earnings.		\$ 5.36	\$ 4.84
Primary earnings		\$ 5.47	\$ 4.95

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Financial Position

(Dollars in thousands)

	Years Ended	February 28 1977	February 29 1976
Working capital provided by:			
Net earnings		\$ 76,759	\$ 69,027
Items not affecting working capital:			
Depreciation		16,669	14,886
Other, net		807	(144)
Operations		94,235	83,769
Disposal of property, plant and equipment		2,263	3,008
Issuance of common stock for conversion of preferred stock—contra below		520	1,746
Issuance of common stock for restricted stock plan		163	—
Issuance of contingent common shares		652	—
Exercise of stock options		2,572	996
Issuance of long-term debt		3,349	1,053
Working capital of purchased companies		5,451	987
To conform pooled companies' fiscal years		—	818
Other, net		—	261
		<u>109,205</u>	<u>92,638</u>
Working capital used for:			
Additions to property, plant and equipment		28,653	21,977
Cash dividends		22,727	18,941
Conversion of preferred stock—contra above		520	1,746
Reduction of long-term debt		4,832	4,454
Purchase of company		8,500	3,000
Purchase and retirement of preferred stock		—	111
To conform pooled company's fiscal year		74	—
Other, net		15	—
		<u>65,321</u>	<u>50,229</u>
Increase in working capital		<u>\$ 43,884</u>	<u>\$ 42,409</u>
Working capital increased (decreased) by:			
Cash and marketable securities		\$ 4,087	\$ 41,154
Receivables		11,814	6,622
Inventories		25,425	27,843
Prepaid expenses and other current assets		2,353	753
Foreign bank borrowings		(7,436)	—
Current maturities of long-term debt		(665)	170
Accounts payable and accrued expenses		10,080	(30,298)
Income taxes		(1,774)	(3,835)
		<u>\$ 43,884</u>	<u>\$ 42,409</u>

See accompanying notes to consolidated financial statements.

Consolidated Statement of Stockholders' Equity

(Dollars in thousands except per share data)

	Preferred Stock	Common Stock	Capital Surplus	Retained Earnings	Total
Balance February 28, 1975:					
As originally reported	\$15,984	\$ 85,862	\$41,778	\$261,932	\$405,556
Adjustments for pooled companies		15,201	(9,488)	47,740	53,453
As restated	15,984	101,063	32,290	309,672	459,009
Net earnings				69,027	69,027
Cash dividends:					
Preferred stock				(791)	(791)
Common stock — \$1.47½ per share				(16,935)	(16,935)
By pooled companies prior to combination				(1,215)	(1,215)
Stock dividends by pooled companies prior to combin- ation—160,912 shares		1,207	1,999	(3,208)	(2)
Purchase and retirement of preferred stock:					
Series B—2,615 shares	(105)		(6)		(111)
Conversion of preferred stock:					
Series B—1,082 shares	(43)	16	27		
Series C—17,032 shares	(1,703)	390	1,313		
Exercise of stock options:					
Common—37,017 shares		278	718		996
Adjustment to conform pooled companies' fiscal years				818	818
Balance February 29, 1976, as restated	14,133	102,954	36,341	357,368	510,796
Net earnings				76,759	76,759
Cash dividends:					
Preferred stock				(729)	(729)
Common stock—\$1.62½ per share				(21,733)	(21,733)
By pooled company prior to combination				(265)	(265)
Stock dividend by pooled company prior to combin- ation—20,185 shares		151	505	(662)	(6)
Conversion of preferred stock:					
Series C—5,196 shares	(520)	119	401		
Exercise of stock options:					
Common—100,945 shares		757	1,815		2,572
Restricted stock plan:					
Common—4,107 shares		31	132		163
Issuance of 18,141 contingent common shares		136	516		652
Adjustment to conform pooled company's fiscal year				(74)	(74)
Balance February 28, 1977	<u>\$13,613</u>	<u>\$104,148</u>	<u>\$39,710</u>	<u>\$410,664</u>	<u>\$568,135</u>

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

February 28, 1977 and February 29, 1976

1. **Significant Accounting Policies**—The company and its subsidiaries employ generally accepted accounting principles on a consistent basis to present fairly their consolidated financial position, results of operations, and changes in financial position. The major accounting policies of the company are set forth below.

Principles of Consolidation—The consolidated financial statements include the accounts of the company and all domestic and foreign subsidiaries, the majority of which are wholly owned. Foreign subsidiaries (principally Canadian) are not material in relation to the consolidated financial position or results of operations. All material intercompany transactions have been eliminated in consolidation.

Fiscal Year—The company's fiscal year ends on the last day of February. In this report, all reference to fiscal 1977 refers to the fiscal year ended February 28, 1977, and fiscal 1976 refers to the fiscal year ended February 29, 1976.

Marketable Securities—Marketable securities, consisting principally of commercial paper, are stated at cost which approximates market.

Inventories—Inventories are stated at the lower of cost (first-in, first-out) or market, except for most footwear manufacturing inventories which are priced on the "last-in, first-out" method of inventory valuation.

Property, Plant & Equipment—Property, plant and equipment is stated at cost, less accumulated depreciation. For financial reporting purposes, the company employs both accelerated and straight-line methods in computing depreciation. Generally, accelerated methods are used for tax purposes and provision is made for deferred income taxes.

Excess of Investment Over Equity in Subsidiaries—Cost in excess of net assets of companies acquired is being amortized on a straight-line basis, generally over 40 years.

Start-Up Expenses—Start-up expenses of new facilities are charged to operations in the year incurred.

Pension Plans—The company's policy with respect to pension plans is to fund pension costs accrued, and to amortize prior service costs, generally over 30 years.

Income Taxes—Investment tax credits are reflected as a reduction of Federal income taxes in the period in which qualified property is placed in service. It is the company's intent that the undistributed earnings of subsidiaries will either be reinvested in the subsidiaries or distributed tax-free to the parent company. Accordingly, no provision has been made for income taxes on such undistributed earnings.

2. **Business Combinations**—During fiscal 1977, the company acquired all the outstanding stock of Sky City Stores, Inc. in exchange for 427,079 shares of the company's common stock. This transaction was accounted for as a pooling of interests; and, accordingly, the accounts of this company have been included in the accompanying consolidated financial statements for fiscal 1977 and fiscal 1976. Consolidated net sales and net earnings for fiscal 1976, prior to restatement for this business combination, were \$1,376,365,000 and \$67,009,000, respectively. The net sales and net earnings of Sky City Stores, Inc. for fiscal 1977, prior to combining, were \$62,189,000 and \$2,512,000, respectively.

Notes to Consolidated Financial Statements

(Continued)

Historically, Sky City Stores, Inc. has reported on a fiscal year ended January 31 of each year. In the consolidated statements of earnings, results for the pooled company for its fiscal years ended January 31, 1977 and 1976 have been included with INTERCO INCORPORATED consolidated results for fiscal 1977 and fiscal 1976, respectively. Retained earnings have been adjusted for the pooled company's operations for the month of February, 1977.

On June 30, 1976, the company acquired Stuffed Shirt/Stuffed Jeans, Inc. (formerly Carlyle Industries, Inc.) for \$8,500,000 cash in a transaction accounted for as a purchase. An additional payment may be made in 1979 based upon the profit performance of the purchased company. The assets and liabilities were recorded at fair values at date of acquisition, and the operating results have been included since acquisition. The results of operations of the purchased company for fiscal 1976 and prior to acquisition in fiscal 1977 are not material to the consolidated statement of earnings.

During fiscal 1976, the company acquired all the outstanding stock of Queen Casuals, Inc. and Londontown Corporation in exchange for 1,780,828 shares of common stock. These transactions were accounted for as poolings of interests. Also, the company acquired Sidney Gould Co., Ltd. in a cash transaction accounted for as a purchase.

3. Inventories—Inventories are summarized as follows (in thousands):

	1977	1976
Finished products-manufacturing	\$ 71,226	\$ 56,394
Retail merchandise	174,840	167,147
Work in process	25,280	23,468
Raw materials	57,278	56,190
	<u>\$328,624</u>	<u>\$303,199</u>

All the major categories of inventory, except retail merchandise, include certain items priced on the "last-in, first-out" method. Had the "first-in, first-out" method been applied to all inventories, they would have been stated at approximately \$353,709,000 and \$326,096,000 at February 28, 1977 and February 29, 1976, respectively.

4. Property, Plant and Equipment—The major classes of property, plant and equipment, at cost, are as follows (in thousands):

	1977	1976
Land	\$ 7,274	\$ 6,343
Buildings and improvements	120,025	103,884
Machinery and equipment	128,540	116,565
Construction in progress	—	8,705
	<u>\$255,839</u>	<u>\$235,497</u>

Construction in progress at February 29, 1976, represented expenditures for the new warehouse and office facilities in Eldersburg, Maryland, which were completed in May, 1976.

Capital expenditures, including construction in progress, amounted to \$28,653,000 and \$21,977,000 for fiscal 1977 and fiscal 1976, respectively.

Approximately 79% and 77% of depreciation expense was computed on the straight-line method in fiscal 1977 and fiscal 1976, respectively. Depreciation charged to operations amounted to \$16,669,000 and \$14,886,000 in fiscal 1977 and fiscal 1976, respectively.

5. **Long-Term Debt**—Long-term debt consists of the following:

	1977	1976
	(In thousands)	
4 $\frac{5}{8}$ % promissory installment notes, payable \$1,875,000 annually, 1977-1989, and balance in 1990	\$36,875	\$38,750
6% promissory installment notes, payable \$1,250,000 annually, 1977-1979, and balance in 1980	5,875	7,125
4 $\frac{3}{4}$ % obligation under long-term lease, payable in annual installments increasing from \$300,000 in 1977 to \$565,000 in 1991	6,345	6,630
Various obligations due cities and other governmental agencies at 1% to 6 $\frac{1}{2}$ %, payable in varying amounts through 1993 . .	5,304	5,000
Foreign mortgages payable with interest rates varying from 12% to 14%, due in 1981	550	630
Other debt at 4 $\frac{1}{2}$ % to 9 $\frac{3}{4}$ % interest rates, payable in varying amounts through 1992	8,200	2,971
	63,149	61,106
Less current maturities	4,778	4,113
	<u>\$58,371</u>	<u>\$56,993</u>

Current maturities of long-term debt in the five fiscal years following 1977, are as follows (in thousands):

1978	\$4,778
1979	4,904
1980	4,854
1981	5,683
1982	<u>4,110</u>

The 4 $\frac{5}{8}$ % note agreement restricts retained earnings of \$43,810,000 as to payment of cash dividends on capital stock and the purchase, redemption or retirement of capital stock. The agreement also provides that no such payments be made unless consolidated working capital shall be at least \$80,000,000.

6. **Preferred Stock**—The company's preferred stock is issuable in series. Authorized preferred stock consists of 577,060 shares of first preferred and 1,000,000 shares of second preferred, both without par value.

At February 28, 1977 and February 29, 1976, the outstanding preferred stock consisted of 136,131 and 141,327 shares, respectively, of Series C, \$5.25 Cumulative Convertible Second Preferred Stock with stated and involuntary liquidating value of \$100 per share.

Subsequent to February 28, 1977, all the Series C Stock was converted into 415,643 shares of common stock at the conversion rate of 3.0534 shares of common stock for each one share of preferred stock, and 19.3954 fractional shares were redeemed for cash.

7. **Common Stock**—The company's common stock consists of 50,000,000 shares authorized with stated value of \$7.50 per share, of which 13,886,459 and 13,727,220 shares were issued at February 28, 1977 and February 29, 1976, respectively.

Shares of common stock were reserved for the following purposes at February 28, 1977:

	Number of Shares
Conversion of preferred stock	415,643
Common stock options:	
Granted	136,978
Available for grant	112,605
Restricted stock plan of pooled company	11,527
	<u>676,753</u>

Notes to Consolidated Financial Statements

(Continued)

Under the company's stock option plans, certain key employees may be granted qualified or non-qualified options to purchase shares of common stock. Qualified options granted under the plans may not be less than 100% of the fair market value of the common stock on the date an option is granted, and non-qualified options at not less than 85%. Qualified options are exercisable at varying dates one year after granting and expire five years after granting. Non-qualified options become exercisable one year after granting and expire ten years after granting. All options which have been granted, qualified and non-qualified, were at 100% of fair market value on the date of grant.

Changes in options granted are summarized as follows:

	1977		1976	
	Shares	Average Price	Shares	Average Price
Beginning of year	228,375	\$20.72	267,785	\$20.33
Options granted	15,450	43.26	11,400	29.50
Options exercised	(100,945)	20.07	(37,017)	20.67
Options cancelled	(5,902)	27.11	(13,793)	20.57
End of year	<u>136,978</u>	<u>23.47</u>	<u>228,375</u>	<u>20.72</u>
Exercisable at end of year	<u>72,467</u>		<u>144,201</u>	

8. Income Taxes—Income tax expense is composed of the following (in thousands):

	1977	1976
Current:		
Federal	\$64,339	\$58,917
State and city	7,301	6,557
Foreign (principally Canadian)	2,083	1,964
	<u>73,723</u>	<u>67,438</u>
Deferred	(148)	193
	<u>\$73,575</u>	<u>\$67,631</u>
Investment tax credits	\$ 1,646	\$ 781

Certain items are recognized for income tax purposes in years other than those in which they are reported in the consolidated financial statements. The tax effect of such differences resulted in net deferred income taxes summarized as follows (in thousands):

	1977	1976
Depreciation	\$ 552	\$ 610
Installment sales	198	118
Valuation reserves and accruals	(636)	(576)
Deferred compensation	157	45
Adjustments resulting from audit of prior years' tax returns	(420)	17
Other	1	(21)
	<u>\$(148)</u>	<u>\$ 193</u>

Future Federal income tax benefits at February 28, 1977 and February 29, 1976 are included in the accompanying consolidated balance sheet as follows (in thousands):

	1977	1976
Prepaid expenses and other current assets	\$4,418	\$4,030
Other assets	1,290	1,530
	<u>\$5,708</u>	<u>\$5,560</u>

The Federal income tax returns of the company and its major subsidiaries have been examined through fiscal year ended February 28, 1974.

9. **Pension Plans**—The company and its subsidiaries have pension plans covering substantially all employees. Total pension expense was \$11,900,000 and \$9,900,000 in fiscal 1977 and fiscal 1976, respectively. As of the most recent valuation dates, the actuarially computed value of vested benefits under defined benefit pension plans exceeded assets of the plans by approximately \$35,900,000.

10. **Lease Commitments**—Substantially all of the company's retail outlets and certain other real properties and equipment are operated under lease agreements expiring at various times through the year 2006. Leases covering retail outlets and equipment generally require, in addition to stated minimums, contingent rentals based on retail sales and equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates.

Total rental expense was as follows (in thousands):

	1977	1976
Basic rentals	\$32,991	\$30,057
Contingent rentals	14,176	12,389
	<u>47,167</u>	<u>42,446</u>
Less sublease rentals	1,288	1,502
	<u>\$45,879</u>	<u>\$40,944</u>

Included in rental expense above is the cost of services provided by lessors of leased retail departments, estimated to aggregate \$6,900,000 and \$6,800,000 in fiscal 1977 and fiscal 1976, respectively.

At February 28, 1977, minimum rental commitments under all non-cancellable leases, excluding capitalized leases, are as follows (in thousands):

Year	Type of Property		Total
	Real Property	Equipment	
1978	\$ 28,128	\$1,794	\$ 29,922
1979	26,093	1,293	27,386
1980	24,354	914	25,268
1981	21,796	618	22,414
1982	19,661	173	19,834
1983-1987	77,577	17	77,594
1988-1992	43,569	—	43,569
1993-1997	15,163	—	15,163
1998-2006	4,126	—	4,126
	<u>\$260,467</u>	<u>\$4,809</u>	<u>\$265,276</u>

The above minimum rental commitments for real property have been reduced by rentals from subleases. These subleases, expiring at various dates to 1994, provide for aggregate minimum rentals of approximately \$4,600,000.

The present value of noncapitalized financing leases, as defined by the Securities and Exchange Commission, was \$48,200,000 and \$39,300,000 at February 28, 1977 and February 29, 1976, respectively. Interest rates ranged from 4.75% to 13.0% with a weighted average rate of 9.4%. The impact on net earnings, if such leases had been capitalized, is not material to the accompanying consolidated financial statements.

The company has also guaranteed leases of certain retail outlets of customers which at February 28, 1977, aggregated approximately \$2,500,000 based on minimum rentals.

Notes to Consolidated Financial Statements

(Continued)

11. Litigation—The company is a defendant and may become a defendant in a number of pending or threatened legal proceedings in the ordinary course of business. In the opinion of management, the ultimate liability, if any, of the company from all such proceedings will not have a material adverse effect upon the consolidated financial position or results of operations.

The Federal Trade Commission is currently investigating the marketing and distribution methods of the women's apparel industry, and a number of the company's women's apparel manufacturing companies have furnished the Commission with information in this regard. A similar investigation has been undertaken with respect to certain footwear manufacturing operations of the company and one men's apparel manufacturing subsidiary. Should the Commission issue a complaint as a result of said investigations, any final resolution of such matters will not have a material adverse effect upon the company.

12. Earnings Per Share of Common Stock—Fully diluted earnings per share are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the years, plus those common shares which would have been issued if conversion of all preferred stock had taken place at the beginning of each year. Common stock options, the exercise of which would result in dilution of earnings per share, have been considered as the equivalent of common stock.

Primary earnings per share are based on those shares included in the fully diluted earnings per share calculations, except that conversion of preferred stock has not been assumed. Net earnings for this computation were reduced by preferred stock dividend requirements.

13. Fiscal 1977 Interim Financial Information (Unaudited)—The following unaudited quarterly information for fiscal 1977 includes all adjustments and is restated to include a combination accounted for as a pooling of interests (in thousands except per share data):

	Three Months Ended			
	May 31 1976	August 31 1976	November 30 1976	February 28 1977
Net sales	\$376,531	\$401,452	\$397,712	\$390,737
Other income	3,933	2,877	3,713	5,891
	<u>380,464</u>	<u>404,329</u>	<u>401,425</u>	<u>396,628</u>
Cost of sales, selling, general and administrative expenses	<u>348,405</u>	<u>369,963</u>	<u>360,225</u>	<u>353,919</u>
Earnings before income taxes . . .	32,059	34,366	41,200	42,709
Income taxes	<u>16,115</u>	<u>17,295</u>	<u>20,248</u>	<u>19,917</u>
Net earnings	<u>\$ 15,944</u>	<u>\$ 17,071</u>	<u>\$ 20,952</u>	<u>\$ 22,792</u>
Net earnings per share on a fully diluted basis	<u>\$1.11</u>	<u>\$1.20</u>	<u>\$1.46</u>	<u>\$1.59</u>
As reported prior to restatement:				
Net sales	\$364,305	\$387,381	\$381,845	
Net earnings	<u>\$ 15,523</u>	<u>\$ 16,537</u>	<u>\$ 20,460</u>	

14. Replacement Cost Data (Unaudited)—During the year, a Securities and Exchange Commission release required many large companies to report certain information relating to replacement cost of inventories and fixed assets, and the impact of these costs upon depreciation and cost of sales.

In the normal course of business, the company has been able and will continue to replace its productive capacity in an orderly manner. Historically, the company has been able to compensate for cost increases through increases in productivity and selling prices in order to maintain an approximately constant gross profit percentage of sales.

Due to inflation and the cost of technological improvements, the replacement of plant and equipment with assets having equivalent productive capacity has usually required a substantially greater capital investment than was required to purchase the assets which were being replaced. The additional capital investment principally reflects the cumulative impact of inflation on the long-lived nature (approximately 10 years for machinery and 25 years for buildings) of these assets.

The company's annual report on Form 10-K (a copy of which is available upon request) will contain more specific information with respect to the year-end 1977 replacement cost of inventories and productive capacity (buildings, machinery, and equipment), and the approximate effect which replacement cost would have had on the computation of cost of sales and depreciation expense for the year.

PEAT, MARWICK, MITCHELL & CO.
Certified Public Accountants
720 Olive Street
St. Louis, Missouri

**THE BOARD OF DIRECTORS AND STOCKHOLDERS
INTERCO INCORPORATED:**

We have examined the consolidated balance sheets of **INTERCO INCORPORATED** and subsidiaries as of February 28, 1977 and February 29, 1976 and the related consolidated statements of earnings, stockholders' equity, and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of **INTERCO INCORPORATED** and subsidiaries at February 28, 1977 and February 29, 1976 and the results of their operations, and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

April 12, 1977

Peat, marwick, mitchell & Co.

Five Year Consolidated Financial Review

(Dollars in thousands except per share data)

	FISCAL YEARS ENDED				
	1977	1976	1975	1974	1973
FOR THE YEAR					
Summary of operations:					
Net sales.	\$1,566,432	\$1,424,252	\$1,373,223	\$1,304,874	\$1,188,426
Cost of sales.	1,094,849	992,778	963,825	921,545	839,208
Interest expense.	4,188	3,710	5,814	5,799	5,036
Earnings before income taxes.	150,334	136,658	121,925	111,318	97,411
As a percent of sales.	9.6%	9.6%	8.9%	8.5%	8.2%
Income taxes.	73,575	67,631	60,255	54,144	48,136
Net earnings.	76,759	69,027	61,670	57,174	49,275
As a percent of sales.	4.9%	4.8%	4.5%	4.4%	4.1%
Earnings applicable to common stock.	76,030	68,253	60,822	56,308	48,291
Per share of common stock:					
Fully diluted earnings (1).	\$5.36	\$4.84	\$4.34	\$4.04	\$3.48
Dividends.	\$1.62 ^{1/2}	\$1.47 ^{1/2}	\$1.43 ^{1/2}	\$1.32	\$1.25
Average common and common equivalent shares outstanding (in thousands) (1).					
	14,324	14,268	14,207	14,140	14,161
Cash dividends paid:					
On common stock.	\$21,998	\$18,150	\$17,270	\$14,418	\$12,542
On preferred stock.	\$ 729	\$ 791	\$ 850	\$ 868	\$ 988
AT YEAR END					
Working capital.	\$483,612	\$439,728	\$397,319	\$363,063	\$333,708
Property, plant and equipment, net.	135,614	122,319	116,563	111,151	97,877
Capital expenditures.	28,653	21,977	22,775	26,439	18,131
Total assets.	778,038	719,344	638,400	624,371	573,952
Long-term debt.	58,371	56,993	60,394	65,193	63,890
Stockholders' equity.	568,135	510,796	459,009	415,479	374,019
Book value per common share.	\$39.93	\$36.18	\$32.88	\$29.78	\$26.86

(1) Refer to Earnings Per Share of Common Stock in Notes to Consolidated Financial Statements.

(2) The above figures have been restated to include pooled companies for years prior to their acquisition.

(3) Fiscal years end the last day in February.

Management's Discussion and Analysis of Operations

Net Sales—Sales for fiscal 1977 again established a new record, an increase of 10.0% over fiscal 1976 compared to a 3.7% increase for fiscal 1976 over fiscal 1975. The first half of the 1977 fiscal year showed stronger improvement reflecting sales increases of 17.2%, as compared to the last half gain of 3.7%. However, the improvement in the last half compares to a very strong 11.0% sales increase in the same period last year.

The Apparel Manufacturing Group showed the greatest improvement for fiscal 1977 with a sales increase of 19.0% compared to an increase of 3.2% in the prior year. The General Retail Merchandising Group attained a sales increase of 5.1% following an 11.4% increase in fiscal 1976. The Footwear Manufacturing and Retailing Group had a sales increase of 5.6% after a 2.6% decrease in sales last year.

Cost of Sales and Operating Expense—Cost of sales and operating expenses combined were 91.2% of sales in both fiscal 1977 and fiscal 1976.

Cost of sales as a percent of sales was slightly higher in fiscal 1977 compared to fiscal 1976. The gross profit of the Apparel and Footwear Manufacturing Groups improved due to the increase in sales and the ability to control the fixed overhead costs. However, this improvement was offset by the increased cost of sales in the General Retail and Footwear Retail Groups which was attributable to above-normal markdowns in an extremely competitive retail environment which existed during the latter part of the year.

Operating expenses were down as a percent of sales, but on a comparative basis increased by 8.9% in fiscal 1977 compared to 3.7% in fiscal 1976. This can be mainly attributed to higher operating costs in most categories and to the severe winter weather which forced the closing of a number of manufacturing units and the curtailment of store hours in some shopping centers and other retail locations.

Interest Expense—Substantially all the interest expense is attributable to the long-term debt including capitalized financing leases of the company. The only short-term debt during either year was of a short-term seasonal nature and the foreign bank borrowing outstanding at year end. Interest expense increased by \$478,000 in the current year. This is the result of a slightly higher long-term debt during the period and the foreign bank borrowing. In fiscal 1976, interest expense decreased by \$2,104,000 due to the reduction in short-term borrowing and the corresponding interest rates.

Earnings Before Income Taxes—Earnings before income taxes increased by 10.0% in fiscal 1977 as compared to a 12.1% increase in fiscal 1976. The increase in fiscal 1977 relates to the percentage increase in sales with cost of sales and operating expenses remaining constant as a percent of sales in both years. In fiscal 1976, the improvement can be attributed mainly to the gross profit improvement and the substantial reduction in interest expense.

Income Taxes—Income taxes for fiscal 1977 increased by 8.8% with an effective tax rate of 48.9% compared to an increase last year of 12.2% and an effective tax rate of 49.5%. After adjustment for investment tax credits received in the respective year, the increases correspond directly to the improvement in pre-tax profit and the effective tax rate is the same in both years.

Board of Directors



RONALD L. AYLWARD



MAURICE R. CHAMBERS



RICHARD P. HAMILTON



PHILIP N. HIRSCH



DONALD E. LASATER



NORFLEET H. RAND



STANLEY M. COHEN

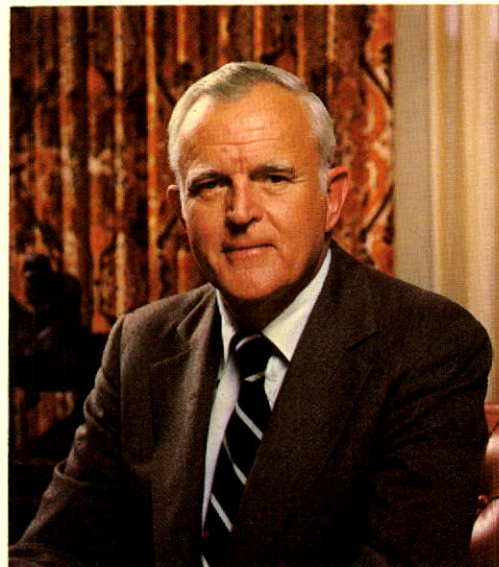


WILLIAM L. EDWARDS, JR.

- * RONALD L. AYLWARD
Vice President and
General Counsel of
the Company
- * MAURICE R. CHAMBERS
Chairman of the Executive
Committee of the
Company
- * STANLEY M. COHEN
President, Central
Hardware Company
- * WILLIAM L. EDWARDS, JR.
Chairman of the
Board and Chief
Executive Officer of
the Company
- RICHARD P. HAMILTON
President, The Florsheim
Shoe Company
- * PHILIP N. HIRSCH
Chairman of the Board,
P. N. Hirsch & Company



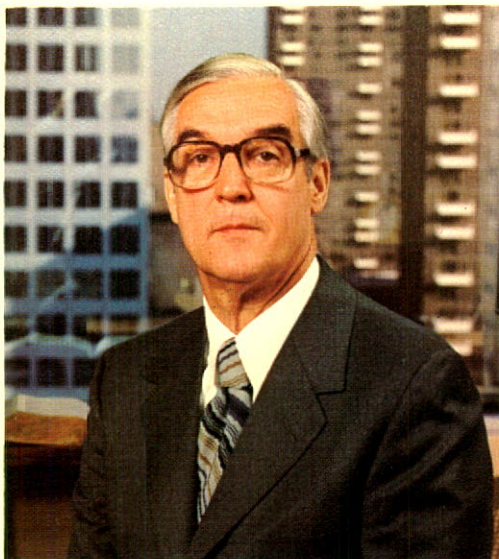
J. LEE JOHNSON



EDWIN S. JONES

- * J. LEE JOHNSON
Retired
- EDWIN S. JONES
Chairman of the Board,
First Union Bancorporation
- DONALD E. LASATER
Chairman of the Board,
Mercantile Bancorporation
Inc. and Mercantile Trust
Company National
Association
- * NORFLEET H. RAND
Retired
- * JOHN K. RIEDY
President and Chief
Operating Officer of
the Company
- HERBERT SHAINBERG
Retired

- * Members of the
Executive Committee of the
Board of Directors



JOHN K. RIEDY



HERBERT SHAINBERG

Audit Committee
J. Lee Johnson, Chairman
Maurice R. Chambers
Edwin S. Jones
Donald E. Lasater
Norfleet H. Rand

**Executive Compensation
and Stock Option
Committee**
Maurice R. Chambers,
Chairman
J. Lee Johnson
Edwin S. Jones
Donald E. Lasater
Norfleet H. Rand

Corporate Officers

WILLIAM L. EDWARDS, JR.
Chairman of the Board and
Chief Executive Officer

JOHN K. RIEDY
President and Chief
Operating Officer

PHILIP N. HIRSCH
Vice President

STANLEY M. COHEN
Vice President

RICHARD P. HAMILTON
Vice President

RONALD L. AYLWARD
Vice President and
General Counsel

DUANE A. PATTERSON
Secretary

EDWARD P. GRACE
Treasurer

STANLEY F. HUCK
Controller

KEITH E. MATTERN
Assistant Secretary

JAMES K. PENDLETON
Assistant Secretary

WILLIAM R. WITHROW
Assistant Treasurer

RUSSELL L. BAUMANN
Assistant Controller

Operating Board

WILLIAM L. EDWARDS, JR.
Chairman of the Board
and Chief Executive
Officer of the Company

JOHN K. RIEDY
President and Chief Operating
Officer of the Company

RONALD L. AYLWARD
Vice President and General
Counsel of the Company

LIONEL BAXTER
President,
Big Yank Corporation

STANLEY M. COHEN
President,
Central Hardware Company

WILLIAM B. COWDEN
President, Cowden
Manufacturing Company

BARRY S. FINE
President,
Fine's Men's Shops, Inc., and
Standard Sportswear, Inc.

RICHARD P. HAMILTON
President,
The Florsheim Shoe Company

GERALD B. HIRSCH
President,
P. N. Hirsch & Company

DONALD G. MacLEOD
President,
Interco Savage Limited

STANLEY MATZKIN
President, Devon Apparel, Inc.

JONATHAN P. MYERS
President,
Londontown Corporation

MYRON C. PETERSON
Chairman of the Board and
President, Sky City Stores, Inc.

J. CARL POWERS
President,
International Shoe Company

HARVEY ROTHENBERG
Chairman of the Board,
Stuffed Shirt/Stuffed
Jeans, Inc.

CHARLES J.
ROTHSCHILD, JR.
President, Campus Sweater
& Sportswear Company

HARVEY SALIGMAN
President, Queen Casuals, Inc.

ARTHUR SIBLEY
President, College-Town, Inc.

JOHN WEIL
President, Eagle Family
Discount Stores, Inc.

Transfer Agents

Manufacturers Hanover
Trust Company
New York, New York

Mercantile Trust Company
National Association
St. Louis, Missouri

Registrars

Morgan Guaranty Trust Company
New York, New York

St. Louis Union Trust Company
St. Louis, Missouri

Dividend Disbursing Agent

Mercantile Trust Company
National Association
St. Louis, Missouri

Independent Accountants

Peat, Marwick, Mitchell & Co.
St. Louis, Missouri

Exchange Listings

Symbol	Listed
ISS	New York Stock Exchange
ISS	Midwest Stock Exchange

Corporate Offices

Ten Broadway
St. Louis, Missouri 63102
(314) 231-1100

Mailing Address:
Post Office Box 8777
St. Louis, Missouri 63102

Principal Companies of INTERCO

Apparel Manufacturing Group

BIG YANK CORPORATION
New York, New York

THE BILTWELL
COMPANY, INC.
St. Louis, Missouri

CAMPUS SWEATER &
SPORTSWEAR COMPANY
New York, New York

COLLEGE-TOWN, INC.
Braintree, Massachusetts

COWDEN MANUFACTURING
COMPANY
Lexington, Kentucky

DEVON APPAREL, INC.
Philadelphia, Pennsylvania

LONDONTOWN
CORPORATION
Baltimore, Maryland

QUEEN CASUALS, INC.
Philadelphia, Pennsylvania

SIDNEY GOULD CO., LTD.
Garden City Park, New York

STUFFED SHIRT/
STUFFED JEANS, INC.
New York, New York

General Retail Merchandising Group

CENTRAL HARDWARE
COMPANY
St. Louis, Missouri

EAGLE FAMILY DISCOUNT
STORES, INC.
Miami, Florida

FINE'S MEN'S SHOPS, INC.
Norfolk, Virginia

GOLDE'S DEPARTMENT
STORES, INC.
St. Louis, Missouri

P. N. HIRSCH & COMPANY
St. Louis, Missouri

SKY CITY STORES, INC.
Asheville, North Carolina

STANDARD SPORTSWEAR,
INC.
Pittsburgh, Pennsylvania

UNITED SHIRT
DISTRIBUTORS, INC.
Detroit, Michigan

Footwear Manufacturing and Retailing Group

THE FLORSHEIM SHOE
COMPANY
Chicago, Illinois

INTERNATIONAL SHOE
COMPANY
St. Louis, Missouri

INTERCO SAVAGE LIMITED
Cambridge, Ontario, Canada

SENACK SHOES, INC.
St. Louis, Missouri

